DIRECT TESTIMONY

OF

JOHN W. FLITTER

ON BEHALF OF

SOUTH CAROLINA ELECTRIC & GAS COMPANY

DOCKET NO. 97-004-E

Q. STATE YOUR NAME AND BUSINESS ADDRESS.

A. John W. Flitter, 1426 Main Street, Columbia, South Carolina.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

I am Manager of the Fossil Hydro Procurement Department of South Carolina Electric & Gas Company (SCE&G).

Q. DESCRIBE YOUR EDUCATIONAL BACKGROUND AND YOUR BUSINESS EXPERIENCE.

A. I graduated from the University of South Carolina in 1966 with a Bachelor of Science Degree in Business Administration; majoring in Accounting. I was employed by South Carolina Electric & Gas Company in September, 1966 in the Budget and Statistic Department. I have held supervisory and management positions with the Company beginning in 1973 that include Supervisor-Accounting Special Studies, Manager-Cost Studies and Load Research, Manager-Rate Regulation, Manager-Fossil Fuel Supply and my current position of Manager-Fossil Hydro Procurement. I have previously presented testimony on numerous occasions before this Commission and the Federal Energy Regulation Commission for both South Carolina Electric & Gas Company and South Carolina Generating Company (GENCO).

Q. SUMMARIZE YOUR DUTIES AS MANAGER OF FOSSIL HYDRO PROCUREMENT AS THEY RELATE TO FOSSIL FUEL.

A. I am responsible for the planning, development, analysis and implementation of system-wide strategies for the purchase and delivery of fossil fuels for electric generation in a manner consistent with the Company's objective to obtain the greatest ultimate value for each dollar spent, consistent with maximum reliability. I also perform these functions for South Carolina Generating Company's (GENCO) Williams Station.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. The purpose of my testimony is to describe procurement and delivery activities for fossil fuel used in electric generation for SCE&G and GENCO.

Q. WHAT ARE THE OBJECTIVES OF THE COMPANY'S FUEL PURCHASING PRACTICES?

A. The objectives of the Company's fossil fuel purchasing practices are to provide a reliable supply, the required quality, and reasonable prices of fossil fuels. These three objectives are inter-related.

Q. HOW DOES THE COMPANY ASSURE THE SUPPLY OF COAL NECESSARY TO ENABLE THE COMPANY TO PROVIDE RELIABLE SERVICE?

A. The strategy to meet this objective is developed based upon our projected burn levels, our anticipated coal inventory levels and the anticipated availability and price of coal in the marketplace. Of course, maximum assurance of supply could be achieved hypothetically by securing contracts for our total requirements. However, doing so would prevent the Company from taking advantage of potentially favorable supply and price changes in the short-term and spot markets. As an effective supplement to our long-term agreements, our short-term contracts have enabled us to assure consistent supplies over a one or two-year period, combining assurance of supply with an ability to meet changing market conditions. In addition, we have maintained an active role in the spot market, making purchases from reliable suppliers to meet our requirements not satisfied by our contracts. Furthermore, our long-term contracts contain variable quantity provisions which enable the Company to increase or decrease contract quantities under certain conditions. This assures us that additional coal will be available under those contracts should it be in our best interest to expand our purchases under them. This also allows us to decrease purchases should our participation in the short-term or spot markets be more advantageous. Finally, we strive to maintain an average coal inventory equal to approximately two (2) months anticipated consumption. This inventory serves several functions. It serves to moderate the overall cost to our ratepayers, while, at the same time, it also protects us against problems in availability, production and deliverability of coal. In some cases, we rely upon inventory to meet supply requirements because of unfavorable market conditions at the time, although such reliance must be exercised with careful consideration of future requirements and operating conditions.

Q. **HOW DOES THE COMPANY ACHIEVE THE OBJECTIVE OF AN ASSURED QUALITY OF THE COAL IT NEEDS?**

A. The Company's contracts for coal supplies and our orders for spot market purchases of coal identify the quality specifications of the coal which it requires. Quality characteristics include: BTU content, moisture content, ash content, ash fusion temperature, volatile, sulfur content, grindability and size. Our contracts for coal supplies and our purchase orders for spot market purchases include upward cost adjustment provisions for shipments which exceed the guaranteed BTU specification and downward cost adjustment provisions for failure of the shipments to meet the guaranteed BTU content. With respect to quality characteristics, our contracts provide for cancellation or rejection, at our option, for failure of the supplier to meet any of the specifications identified in the contract. With respect to spot market deliveries, the failure of the supplier to meet any of the required specifications can result in the cancellation or rejection of deliveries under the purchase order.

Q. **HOW DOES THE COMPANY EVALUATE THAT PART OF THE COMPANY'S PURCHASING OBJECTIVE RELATED TO "REASONABLE PRICE"?**

A. In our analysis of fuel purchasing, the reasonableness of the price which we pay for coal cannot be realistically separated from the assurance of an adequate supply of coal meeting our quality specifications. Price is a concept contingent on supply, quality and location and is ultimately related to the value of the coal in the operation of our generating plants, expressed on the basis of cost per MBTU. Price incorporates the cost of fuel, pricing mechanisms and transportation, and must be evaluated under market conditions which are current at the time of the establishment of the price. For example, under certain market conditions, the establishment of a firm price per ton for coal may be preferable to a price which is adjusted periodically based on independent indexes. Under other conditions, the periodic adjustment mechanism may be preferable. Furthermore, it can be considered advantageous to have a variety of pricing mechanisms among coal contracts in order to mitigate or avoid the effects on prices produced by changes in market conditions or indexes which would be exaggerated if pricing mechanisms were identical ~~in~~ all coal contracts.

Another consideration in pricing is the information concerning various market conditions which can be useful in evaluating the reasonableness of price. We continually review published data from a variety of public and governmental sources, and are in continuous contact with market participants who provide information concerning various market conditions which we evaluate carefully for our purchasing decisions. Such market data is used in our analysis of current or prospective coal costs to illustrate whether those costs are generally comparable to the market. Because prices are contingent upon current, and to some extent, projected, market conditions and factors unique to each buyer, a simple comparison of coal costs experienced by several purchasers, even electric utilities in the same geographic region, would not itself establish the reasonableness of the prices paid for coal supplies. In the final analysis, there is no single gauge or standard against which to measure the reasonableness of a particular price. Rather, price must reflect the value of the fuel, the supply requirements and quality considerations of the buyer, and the corresponding economic and supply conditions in the marketplace at the time a contract is made. In light of those considerations, the Company has been able to achieve its coal purchasing objective at a reasonable cost to the Company and its customers.

Q. **SUMMARIZE THE QUANTITY, QUALITY, AND TERM OF THE COMPANY'S COAL CONTRACTS.**

A. During the period March, 1996 through February, 1997, the Company purchased approximately 5.1 million tons of coal under long term and short term contracts which represented approximately 92.4% of the requirement for the Company's five coal-fired stations, GENCO's Williams Station and Savannah River Site. The Company presently has coal under long term contract with six suppliers for 4.39 million tons annually. For the March, 1997 through February, 1998 period, the Company projects to receive approximately 4.9 million tons of coal under long term and short term contracts which represents approximately 86.96% of the estimated requirement for the period. The quality ranges are from 12,600 to 13,000 BTU with a sulfur content of from 0.75% to 2.0%. These contracts are for periods of from one (1) to three (3) years with options to renew or extend for as long as six (6) additional years. The amount of coal under contract will vary from year to year. In our coal contracts, we have been successful in negotiating pricing adjustments whereby the price is not changed for a fixed period of time, usually semiannually or annually. Normally these price adjustments are based on either a predetermined adjustment amount or independent indexes found in Employment and Earnings and Producer Price Indexes, published monthly by the U.S. Department of Labor, Bureau of Labor Statistics. These indexes reflect changes in mining costs to include labor, fuel, explosives, power, equipment, and supplies.

Q. **WHAT PRICES HAS THE COMPANY PAID FOR ITS COAL FROM MARCH 1996 THROUGH FEBRUARY 1997?**

A. Exhibit No. ________ (JWF-1) entitled, "Coal Purchased For Steam Plants", shows the average cost per MBTU of coal purchased in March, 1996 through February, 1997. Based on the long term and short term contracts and the purchases of spot coal during that period, we have seen the cost of coal vary in price from a high of $1.0480 per MBTU ($26.80 per ton) in June 1996 to a low of $1.0255 per MBTU ($26.16 per ton) in January 1997.

Q. **HOW HAVE FREIGHT COSTS VARIED FROM MARCH 1996 THROUGH FEBRUARY 1997?**

A. My Exhibit No. ___________ (JWF-1) shows the average freight costs per MBTU for coal purchased for each month. During that period, the freight costs varied from a high of $0.5419 per MBTU ($13.82 per ton) in January 1997 to a low of $0.5251 per MBTU ($13.42 per ton) in August 1996.

Q. **HOW HAVE DELIVERED COSTS FOR COAL TO INCLUDE FREIGHT VARIED FROM MARCH 1996 THROUGH FEBRUARY 1997?**

A. Exhibit No. ________ (JWF-1) shows the average delivered cost per MBTU of coal purchased in March, 1996 through February, 1997. During that period, we have seen the delivered cost of coal vary in price from a high of $1.5832 per MBTU ($40.53 per ton) in May 1996 to a low of $1.5608 per MBTU ($39.89 per ton) in February 1997.

Q. WHAT FREIGHT RATE CHANGES HAS THE COMPANY EXPERIENCED?

A. During the period under review for this proceeding, the Company experienced no increase in its freight rates for the period beginning March, 1996 through February, 1997 for the transportation of coal.

Q. WHAT HAS THE COMPANY DONE TO INSURE THAT THE COSTS FOR FREIGHT ARE FAIR AND EQUITABLE?

A. We are continually communicating with our freight carriers regarding innovative ways by which we can moderate not only present but also future freight costs for the movement of coal to our Company. The Company is addressing various issues with CSX Transportation, Inc. and the Norfolk Southern Corporation to include increased freight rate discounts, minimized future freight rate adjustments, and increased incentives for additional tonnages moved. The Company is also investigating the feasibility of various alternatives for the transportation of coal supplies to our stations. We will continue to investigate and take advantage of every opportunity to ensure that our freight costs are at the lowest possible level.

Q. HAS SCE&G MADE EVERY REASONABLE EFFORT TO MINIMIZE ITS FUEL PROCUREMENT COSTS?

A. Yes. As outlined above, we have made every reasonable effort to obtain reliable, high quality suppliers of fuel and transportation at the lowest possible cost to our customers.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

Exhibit No. ________ (JWF-1)

South Carolina Electric & Gas

COAL PURCHASED FOR STEAM PLANTS

March 1996 THROUGH FEBRUARY 1997